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International Aspects of Roosevelt's Monetary Policy

by

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with the aid of the Research Staff of the Foreign Policy Association

ADOPTION by Congress on January 27 of the Gold Reserve Act of 1934 embodying the recommendations contained in President Roosevelt's message of January 15 marked the crystallization of the monetary phase of the Administration's domestic recovery program. Among the chief provisions of this act were: (1) acquisition by the Treasury of all the monetary gold in the United States; (2) fixing an upper limit on the permissible revaluation of the dollar at 60 per cent of its former parity; (3) utilization of $2,000,000,000 of the profits obtained through the revaluation of the government's gold stocks for the establishment of an equalization fund to steady the foreign exchange rate of the dollar.[1] While these steps removed much of the uncertainty which had surrounded the Administration's monetary program during the previous ten months, they represented a compromise rather than an abandonment of the policy of dollar depreciation followed in the earlier period. As far as immediate effects are concerned, the setting of the upper limit of devaluation at 60 per cent of the former dollar value has served to depress American currency even more successfully than the previous gold purchasing policy, and thus intensified international friction. The noteworthy omission of all mention of price raising in the President's message, on the other hand, together with the reference to "a less variable purchasing power of the dollar" and the establishment of an equalization fund, appears to indicate a growing recognition of the importance of exchange stability as contrasted with regulation of the domestic price level.

It was logical that in the national recovery program emphasis should be placed on monetary policy, because the generally accepted theory of the depression stressed the importance of deficient consumer purchasing power and the crushing burden of indebtedness. But the urgency under which the program was formulated prevented full consideration of its possible international repercussions. For a time, in fact, the inconsistency between a recovery plan drawn up along nationalist lines and the traditional internationalist policies of the Democratic party did not become apparent. By actively participating in the London Economic Conference, the Administration was obviously seeking to lay the groundwork for world recovery through a reversal of the trend toward economic nationalism. That this attempt was shattered by the exigencies of domestic monetary policy is now generally recognized.[2] A choice had to be made, and the President's statement of July 2 left no doubt as to the nature of the decision. It is the purpose of this report to examine the implications of that decision on the prospects for world recovery in the light of present-day economic trends.

SUSPENSION OF THE GOLD STANDARD

Following his inauguration, President Roosevelt's first official act was the proclamation of a national bank holiday which embodied among its provisions an embargo on gold exports and the prohibition of all dealings in foreign exchange.[3] The reason for this drastic action was clear. During February and the first four days of March, there had been a net decline of $306,000,000 in American gold stocks, due to export or earmarking for foreign account. An additional $318,000,000 had been withdrawn for hoarding within the country.[4] Although the remaining gold reserves of $2,853,000,000 were considerably greater than had been held by the United States at any time prior to 1922[5] and were well above legal requirements, the collapse of the American banking structure gave reason to fear that a continued withdrawal of gold might have a detrimental effect on public confidence. The embargo was modified somewhat by an executive order of March 10 permitting the export of gold under license, but little was actually exported under this arrangement. Gradually the pressure on reserves subsided. By April 5 the return of hoarded gold had increased the gold

1. For full text of the President's message and the Administration's bill as introduced into Congress, cf. *New York Times*, January 16, 1934.

2. Cf. M. S. Stewart, "The Work of the London Economic Conference," *Foreign Policy Reports*, November 8, 1933, p. 198, 200-2.

3. For text of the President's proclamation of March 6, 1933, cf. *Federal Reserve Bulletin*, March 1933, p. 113.

4. *Ibid.*, April 1933, p. 215.

5. *Ibid.*, p. 259-60.

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stock in the vaults of the Federal Reserve Banks and the Treasury to $3,538,000,000, while the total gold holdings in the United States had been raised to $4,300,000,000, which constituted over 36 per cent of the world's supply of monetary gold.[6]

Meanwhile, despite the fact that this country was technically off the gold standard, the exchange rate of the dollar remained practically at par. Uncertainty regarding the stability of American currency suddenly reappeared in mid-April,[7] however, as the result of the rapid growth of sentiment in Congress for direct monetary inflation. This anxiety was accentuated on April 17 by the narrow defeat, 43 votes to 33, of the Wheeler amendment to the farm relief bill which would have remonetized silver at the ratio of 16 to 1.[8] As the licensing of small amounts of gold for export had not checked the decline of the dollar,[9] the Administration was forced to choose between restoring full gold convertibility and definitely abandoning the attempts to maintain exchange stability. The decision was quickly reached. On April 19 President Roosevelt announced that no further licenses for gold exports would be granted, and Secretary Woodin admitted for the first time that the United States had suspended the gold standard.[10]

Explanations differ regarding the grounds for this action, but subsequent events indicate that it was the result of a considered policy[11] rather than an emergency measure. While it is impossible to estimate accurately the amount of gold which might have been lost if this country had restored gold convertibility at the existing parity, the consensus of opinion is that it would have been relatively small. With the exception of a brief period preceding England's departure from the gold standard, the gold holdings of the Federal Reserve System on April 19 were the highest in its history.[12] Foreign balances had been largely withdrawn prior to the bank holiday, and most of the $600,000,000[13] which remained was required for the maintenance of normal trade activities.[14] Under the circumstances, therefore, the allegation that a group of international speculators were striving to depress the dollar[15] carries no weight, for a determined effort to support the dollar would have brought them heavy losses, while to give way was to play into their hands. Fear lest the growth of inflationary sentiment in Congress would result in its getting out of control was undoubtedly a more important factor,[16] but there is little evidence that inflationary legislation could have been adopted over the President's veto had he chosen to oppose it.[17] Nor does there seem to be much basis for the contention that the action would strengthen the "bargaining power" of the United States at the discussions which were to open a few days later with Prime Minister MacDonald and M. Herriot.[18] Instead of reinforcing the American position, there was always the danger, as was borne out by subsequent events, that the abandonment of gold would prove an insuperable barrier to the success of the negotiations.[19] Not only were the technical problems involved in stabilization greatly aggravated by wide fluctuations in exchange, but the deliberate depreciation of the dollar was almost certain to provoke nationalist feelings and make a settlement of the outstanding issues vastly more difficult.[20]

It may be safely assumed, therefore, that the chief purpose of the gold embargo was to increase domestic prices with a view to stimulating general economic activity. The raising of the price level was considered necessary, both as a means of increasing the purchasing power of producers of primary commodities and of diminishing the relative burden of fixed indebtedness. The critical situation with regard to farm mortgages was of particular concern,[21] since it affected not only the farmers, but a large proportion of the assets of many banks and insurance companies. The inadequacy of world gold stocks convinced certain observers that a return to the price level of 1922-1929 was impossible at the existing dollar parity, unless it was brought about by some unusual and spectacular decrease in the demand for monetary gold.[22] To have raised prices by direct "reflationary" action without abandoning the gold standard would have been relatively ineffective, it was argued, because the added purchasing power would largely be diverted toward increasing imports at the expense of

6. *Ibid.*, May 1933, p. 279, 293.
7. At least one foreign critic maintains that the decline was deliberately manipulated in order to give the United States an excuse for abandoning gold. Cf. P. Einzig, *The Sterling-Dollar-Franc Tangle* (New York, Macmillan, 1933), p. 74-75.
8. At the prices prevailing on April 17, the market ratio between gold and silver was over 72 to 1.
9. On April 18 the franc closed at 4.03 cents, well above the gold point.
10. Cf. *New York Times*, April 20, 1933; for text of Executive Order of April 20 forbidding gold exports, cf. *Federal Reserve Bulletin*, May 1933, p. 266.
11. Cf. *The Economist*, April 22, 1933; also E. K. Lindley, *The Roosevelt Revolution* (New York, Viking Press, 1933), p. 77.
12. Weekly report of the Federal Reserve Banks, *New York Times*, April 21, 1933.
13. Cf. *New York Times*, April 22, 1933.
14. Cf. article by E. V. Bell, *ibid.*, April 23, 1933; also *The Economist*, April 22, 1933, p. 849.
15. Cf. Lindley, *The Roosevelt Revolution*, cited, p. 117-8.
16. For description of the political factors influencing the Administration, cf. Lindley, *The Roosevelt Revolution*, cited, p. 116-21.
17. Cf. article by Arthur Krock, *New York Times*, December 27, 1933.
18. *New York Times*, April 20, 1933.
19. Cf. *Foreign Policy Bulletin*, April 28, May 5, June 16, 23, 1933.
20. Cf. M. S. Stewart, "The Problems before the World Economic Conference," *Foreign Policy Reports*, June 7, 1933, p. 75.
21. Cf. *The Internal Debts of the United States*, edited by Evans Clark (published for the Twentieth Century Fund by the Macmillan Company, 1933).
22. Cf. paper presented by George F. Warren and F. A. Pearson before the American Economic Association (*New York Times*, December 29, 1933).

domestic products.[23] Once a nation has abandoned a fixed monetary standard, the value of its currency is determined by the balance between incoming and outgoing payments, and this fluctuation constitutes an automatic factor protecting the domestic economy against a sudden change in its trade position.

While suspension of the gold standard by the United States was not wholly unexpected in Europe, the immediate reaction of almost all foreign observers was hostile. The American action was compared with that of Great Britain when it was forced to abandon gold, with the implication that the United States had been guilty of bad faith in acting before its reserves were exhausted.[24] The fact that it was the first time in history that a nation had gone off the gold standard except under great pressure led some critics to declare that a death blow had been dealt to the gold standard system itself.[25] Fear was also expressed that by introducing a new element of uncertainty into the world economic situation, the action would indefinitely delay the long-anticipated revival of international trade.[26] Foreign resentment was especially bitter because of the belief that the dollar had been deliberately cheapened to give the United States a temporary advantage in competition for the world's markets. To the extent that the depreciation of the dollar was unaccompanied by "reflationary" measures in the United States, this charge was at least plausible.[27] As the United States maintained a favorable balance of trade during the period, the steady decline of the dollar was apparently due entirely to speculation and the flight of American capital, both induced by fear of inflation.

Inflationary Provisions in the Farm Act

Anxiety regarding the ultimate fate of the dollar was greatly increased in early May when, with the Administration's approval, the Agricultural Adjustment Act was amended to permit a "controlled inflation" by authorizing the President, at his discretion,

a. To request that the Federal Reserve Banks purchase treasury certificates or other federal obligations up to a total of $3,000,000,000 irrespective of safeguards provided by previous laws.

b. To direct the issue of United States notes to an amount not exceeding $3,000,000,000 for the purpose of retiring federal bonds.

c. To adjust the value of the dollar by fixing its gold content or by permitting unlimited coinage of gold and silver at a fixed ratio, with the exception that in no event shall the weight of the gold dollar be reduced by more than 50 per cent.[28]

The powers conferred on the Chief Executive under this measure were without precedent in the history of democratic governments. Under its provisions the President not only had wide latitude in adjusting the value of the dollar, but could base the nation's monetary system on any one of several radically different schemes. He was empowered to restore the gold standard at its former parity or to reduce the gold content of the dollar by any fraction up to one-half; or he could, through his authority to fix the price at which silver might be accepted for unlimited coinage, establish either a bimetallic or a silver standard. Furthermore, by ignoring the clauses relating to a metallic base for the dollar, he could place the currency on an entirely paper basis, either "managed" by control over the volume of currency in circulation and "open-market operations"; or, by issuing fiat currency, he could make uncontrolled inflation inevitable. As against this, however, the act instructed the Secretary of the Treasury to maintain all forms of money at parity with gold.

Abrogation of the Gold Clause

A final step in the renunciation of the gold standard was taken by the passing on June 5 of a joint resolution of both Houses of Congress nullifying the "gold clause" in all existing and future contracts. This step was deemed necessary because the bulk of the fixed debt incurred in the United States, both foreign and domestic, was expressed in dollars of a prescribed gold content.[29] Unless this situation was changed, abandonment of the gold standard would not have had the desired effect of reducing the debt burden.

Although repudiation of the clause was clearly within the powers of the government as far as domestic debts were concerned, the refusal of the United States to maintain gold payments on obligations to foreign nationals created a considerable amount of ill-will abroad on the ground that this country had deliberately dishonored its solemn pledge.[30] This view was considerably moderated, however, upon the somewhat tardy realization of the fact that the United States, as a creditor nation, stood to lose far more on its outstanding private and intergovernmental debts than it could hope to gain in the way of relief on its relatively unimportant obligations to foreigners.[31]

23. It will be readily seen that this view, which was widely held at the time, ignores America's creditor position and discounts the stimulus to exports which would result from increased purchases by the United States. (Cf. M. S. Stewart, "American Commercial Policy and the World Crisis," *Foreign Policy Reports*, May 25, 1932.)

24. Cf. especially *The Morning Post* and *The Times* (London), April 20, 1933.

25. Cf. Einzig, *The Sterling-Dollar-Franc Tangle*, cited, p. 76-7.

26. Cf. *Financial News* (London), April 20, 1933; also article by Viscount Snowden, *New York Times*, May 12, 1933.

27. Between April 19 and July 1 the exchange value of the dollar declined 21.5 per cent in terms of gold, while the index of wholesale commodity prices had risen less than 12 per cent.

28. Agricultural Adjustment Act, 73rd Congress, H. R. 3835, approved May 12, 1933.

29. It has been estimated that about 95 per cent of all publicly offered securities in the United States, totalling upward of fifty billions of dollars in face value, contain the gold clause. A. Nebolsine, "The Gold Clause in Private Contracts," *Yale Review*, May 1933.

30. Cf. *The Morning Post* and *The Financial News* (London), May 2, 1933.

31. Cf. letter of F. H. Hamilton, *The Times* (London), May 6, 1933.

PROPOSED STABILIZATION AT THE LONDON CONFERENCE

The uneasiness of foreign nations regarding the effects of American monetary policy overshadowed all other questions at the opening of the Monetary and Economic Conference at London on June 12. Realizing that *de facto* stabilization was of primary importance if progress was to be made in dealing with tariffs, exchange restrictions and other problems before the Conference, representatives of the leading powers attempted during the first week to formulate an exchange agreement. A major obstacle to this task was the wide difference of opinion in regard to a satisfactory ratio between the dollar and the various foreign currencies. At the beginning of the Conference it was reported that representatives of the United States would insist that the dollar should be stabilized at a par value of at least $4.30 to the pound. The British, on the other hand, estimated that the true value of sterling as determined by comparative prices and wages should be between $3.60 and $3.80;[32] and, having suffered acutely from the overvaluation of the pound in 1926, were determined not to repeat their error by stabilization at the relatively high figure set by the American delegates. For a time, however, it appeared as if an agreement might be reached. On June 15, it was unofficially reported that the governors of the Federal Reserve Bank of New York, the Bank of England and the Bank of France, aided by representatives from the respective treasuries, had worked out a provisional scheme for cooperation in the management of national equalization funds with a view to eliminating extreme fluctuations in currencies.[33] The plan does not appear to have provided for definite stabilization, but its acceptance would naturally have involved a pledge by the United States not to exercise, for the time being at least, the inflationary powers vested in the President by the Agricultural Adjustment Act. While such a commitment would have had a highly beneficial effect on the negotiations in London, Wall Street's reaction to the rumored agreement was extremely disquieting to the Administration. Stock and commodity prices had risen to heights unwarranted by prevailing business conditions in anticipation of currency inflation, and the report that the pound-dollar exchange rate had been temporarily fixed at $4.05 precipitated a severe recession in prices on all markets which was checked only after Secretary Woodin had denied knowledge of such an arrangement. Two days later it was admitted that a plan for currency stabilization had been submitted to President Roosevelt, but in a form unacceptable to the American government.[34] That the collapse of the stock market had materially influenced the Administration's decision was indicated by the statement issued in London on June 22 by the American delegation, in which the United States defended its action on the ground that "its efforts to raise prices are the most important contribution that it can make, and that anything that would interfere with these efforts and possibly cause a violent price recession would harm the Conference more than the lack of an immediate agreement for temporary stabilization."[35]

The determination of the United States to pursue a nationalist monetary policy became even more evident a few days later when the financial experts at London; faced by the threatened break-up of the Conference, sought to find a formula placating the countries which had remained on a gold basis without interfering with the American domestic program. After several days of negotiation a statement was prepared which gained the tentative approval of the President's personal representative, Assistant-Secretary Moley. Carefully phrased so as not to hinder the President in the full use of the inflationary powers which had been placed in his hands, the declaration reaffirmed the intention of the governments which had suspended the gold standard "without in any way prejudicing their future ratios to gold . . . to bring back an international standard based on gold," and as a temporary expedient "to adopt such measures as they may deem most effective to limit exchange speculations."[36] To the surprise and consternation of the Conference, this compromise statement was also emphatically rejected by President Roosevelt. In explanation of his action the President dispatched a note, dated July 2, in which the Administration's monetary policy was for the first time set forth in detail:

> ". . . . The sound internal economic system of a nation is a greater factor in its well-being than the price of its currency in changing terms of the currencies of other nations . . . . So too, old fetishes of so-called international bankers are being replaced by efforts to plan national currencies with the objective of giving to those currencies a continuing purchasing power which does not greatly vary in terms of the commodities and need of modern civilization. Let me be frank in saying that the United States seeks the kind of a dollar which a generation hence will have the same purchasing and debt-paying power as the dollar value which we hope to attain in the near future."[37]

This statement created a sensation, both because of the undeniable asperity of its tone and the unorthodox nature of the views ex-

32. Cf. *The Economist* (London), June 17, 1933, p. 1289-90.
33. Cf. *New York Times*, June 16, 1933.
34. *Ibid.*, June 18, 1933.
35. Department of State, *Press Releases*, June 24, 1933.
36. For text, cf. *New York Times*, July 2, 1933.
37. Department of State, *Press Releases*, July 8, 1933.

pressed. Strangely enough, however, the full implications of the declaration were not generally understood at the time. Many observers were so steeped in traditional monetary theory that they failed to note that "a dollar which a generation hence will have the same purchasing and debt-paying power" as in the near future quite obviously could not be a dollar of fixed gold content. While nothing in the previous pronouncements of the President or his chief advisers had indicated a permanent abandonment of the gold standard, it was now implied that a return to gold would be inconsistent with the Administration's fundamental purpose—the long-range stabilization of the commodity price level—an objective which could be attained only by the retention of complete independence in the management of American currency. To a certain extent these obvious implications were modified by a second statement, issued by the American delegation on July 5 with a view to conciliating foreign opinion. While reaffirming the necessity for raising domestic prices, this statement declared that the United States was willing to associate itself with the British government in asserting that "although a return to the gold standard might be our ultimate objective . . . we must reserve complete liberty to choose both our own time and parity."[38] This pledge of allegiance to gold was so qualified, however, that it marked no essential change in viewpoint from that of the earlier statement.[39]

Although public opinion on the Continent was almost unanimously opposed to American monetary policy as defined by the Administration, many British observers expressed sympathy with the President's view that stability of the internal purchasing power of a currency is of greater importance than stability in terms of foreign exchange.[40] Official British policy was similar to that of the United States in stressing the necessity of raising commodity prices, but differed in that it favored a restoration of the gold standard under which international cooperation would be "secured and maintained with a view to avoiding, so far as . . . practicable, undue fluctuations in the purchasing power of gold."[41]

SECOND STATEMENT ON MONETARY POLICY

Despite Mr. Roosevelt's explicit statement to the London Economic Conference, the greatest confusion regarding American monetary policy prevailed throughout the late summer and early fall. On the assumption that the President's emphasis on price-raising meant that inflationary action was imminent, business activity continued to increase in early July in line with the rise in speculative prices.[42] Late in the month it became apparent that the speculative movement had over-reached itself and a sharp decline on the stock market was followed by a somewhat more gradual decrease in industrial activity.[43] Rumors of inflation re-appeared in early October, but the announcement on October 11 of the refunding of approximately one-third of the outstanding bonds of the Fourth Liberty Loan at a considerable reduction in interest led most observers to believe that the Administration had definitely decided against such a policy.[44] As a result the dollar, which had been gradually drifting lower since its recovery in July, rose abruptly to over 71 per cent of its gold value. A renewed drift toward deflation was abruptly checked, however, on October 22 when President Roosevelt, in a nation-wide radio talk, reaffirmed the government's price-raising policy:

> "Finally, I repeat what I have said on many occasions, that ever since last March the definite policy of the Government has been to restore commodity price levels . . . .
>
> "Some people are putting the cart before the horse. They want a permanent revaluation of the dollar first. It is the Government's policy to restore the price level first. I would not know, and no one else could tell, just what the permanent valuation of the dollar would be. To guess at a permanent gold valuation would certainly cause later changes caused by later facts.
>
> "When we have restored the price level, we shall seek to establish and maintain a dollar which will not change its purchasing and debt-paying power during the succeeding generation . . . .
>
> "Because of conditions in this country and because of events beyond our control in other parts of the world, it becomes increasingly important to develop and apply the further measures which may be necessary from time to time to control the gold value of our own dollar at home. Our dollar is now altogether too greatly influenced by the accidents of international trade, by the internal policies of other nations and by political disturbance in other continents. Therefore the United States must take firmly in its own hands the control of the gold value of our dollar . . . .
>
> "As further effective means to this end, I am going to establish a government market for gold in the United States . . . at prices to be determined from time to time after consultation with the Secretary of the Treasury and the President. Whenever necessary to the end in view, we shall also buy or sell gold in the world market.
>
> "My aim in taking this step is to establish and maintain continuous control. This is a policy and not an expedient. It is not to be used merely

38. *Declaration by the United States Delegation* (Conf. M.E. 14); text also found in *New York Times*, July 6, 1933.

39. Cf. Lindley, *The Roosevelt Revolution*, cited, p. 213-4.

40. Cf. especially "The American Monetary System," and "The Fruits of the World Conference," Midland Bank, *Monthly Review*, July-August, August-September, 1933; and J. M. Keynes, *New York Herald Tribune*, July 4, 1933.

41. Manifesto issued by the British Empire delegations at the World Economic Conference, *The Times* (London), July 28, 1933.

42. The adjusted index of industrial production in the United States for July reached 100 on the basis of the 1923-1925 average, as compared with 60 in March and 58 in July 1932. (*Federal Reserve Bulletin*, November 1933.)

43. The adjusted index of industrial production fell from 100 in July to 91 in August, 84 in September and 77 in October.

44. *Commercial and Financial Chronicle*, October 14, 1933.

to offset a temporary fall in prices. We are thus continuing to move toward a managed currency . . . ."[47]

The immediate effect of the President's speech was to intensify the confusion over the government's monetary policy. Although the goal had been clearly defined, there was still great uncertainty as to the means that would be employed for achieving this objective. In the hope that a re-emergence of inflationary psychology would be sufficient to stimulate prices, the President's first step was to empower the Reconstruction Finance Corporation to purchase gold from domestic producers at a price somewhat above that prevailing abroad. This was carried into effect on October 25 when the R. F. C. announced that it would purchase domestic gold at $31.36 per ounce, which was 27 cents higher than the price quoted at London;[48] and on each of the days immediately following this price was raised slightly. While this indication of the government's determination to reduce the gold value of the dollar even beyond its current depreciation served to check the decline in commodity prices, it proved wholly ineffective as a means of inducing a general rise in the price level;[49] and on October 28 the Administration decided to set up machinery under which the R. F. C. would be enabled to buy gold on the world market.[50] Although the amount of gold actually obtained under this arrangement is believed to have been relatively small,[51] the adoption of this more drastic policy greatly intensified the flight of American capital and thereby drove the dollar to an unprecedented discount of 41½ per cent on November 16.[52] Following rumors of pending measures to restrict capital exports, this decline was checked and the dollar recovered substantially in spite of a continued marking-up of the R. F. C. price for domestic gold. Gradually the daily increase in this quotation was tapered off, however; the price of $34.01 was established on December 1 and remained unaltered until December 17, when it was raised to $34.06.

Silver Purchases

Despite the Administration's efforts to obtain higher commodity prices, the general trend of prices in the latter half of November and early December once more turned downward. In an effort to combat this tendency, President Roosevelt issued a proclamation on December 21 authorizing the Treasury, beginning January 1, to purchase newly mined domestic silver at 64½ cents an ounce. While this step was taken in fulfillment of the international silver agreement signed at London on July 22, in which the United States agreed to buy 24,421,410 ounces annually in return for a restriction of sales by the Indian government,[53] it went beyond the terms of that pact in setting no limit on the amount of silver to be purchased and in fixing a price approximately 50 per cent above the market level. To the extent to which it is effective, it thus marked the first definite inflationary move to be taken under the terms of the Thomas amendment to the farm act. Its purpose, according to the President, was to aid in the "stabilization of domestic prices . . . to protect our foreign commerce against the adverse effect of depreciated currencies," and to enhance and stabilize the world price of silver in order "to augment the purchasing power of silver-using countries."[54]

While the rehabilitation of buying power in the silver-producing states was hailed by representatives of the silver interests as an important step toward national recovery,[55] most economists were inclined to discount the effect of the action both on commodity prices and on the world price of silver. As evidence of its insignificance as a "reflationary" move, critics pointed to the fact that the purchase of the entire domestic production in 1932 at the price specified would have involved an expenditure of less than $15,000,000, which was only three-tenths of one per cent of the current monetary circulation.[56] They maintained that, as the silver pact provided for a substantial increase in the sales of the Indian government,[57] the effect on the world price of silver would be largely psychological. Should a price increase take place, however, critics declared that the effect on the principal silver-using countries would be detrimental rather than beneficial. Since the buying power of a nation depends on the size of its exports, a sudden increase in the exchange value of its currency is likely to impair its competitive position and thereby reduce its ability to secure needed imports. Chinese monetary experts are reported to be especially concerned lest a sudden rise in the value

47. *New York Times*, October 23, 1933.
48. *Commercial and Financial Chronicle*, October 28, 1933.
49. The Labor Bureau's index of commodity prices rose from 70.4 for the week ending October 21 to 70.9 for the week ending October 28.
50. *New York Times*, October 29, 1933.
51. Expenditures for gold up until December 31 by the R.F.C. totalled $78,726,187.37 of which approximately $60,000,000 was spent abroad (*New York Times*, January 10, 1934).
52. In the middle of November it was estimated that the total flight of capital from the United States in the previous three months had been approximately $1,000,000,000 (*New York Times*, November 17, 1933).

53. For details, cf. Stewart, "The Work of the London Economic Conference," cited, p. 203-4.
54. For full text of proclamation, cf. *New York Times*, December 22, 1933.
55. Cf. statements by Senator Pittman and others, *New York Times*, December 22, 1933.
56. Cf. article by E. H. Collins, *New York Herald Tribune*, December 26, 1933.
57. Sales by the Indian government for the four and a half years ending June 30, 1932 averaged 22 million annually, as against 35 million allowed by the Silver Pact. Cf. Bratter, "The Silver Market," U. S. Department of Commerce, *Trade Promotion Series No. 139*, 1932; and Hardy and Harman, *Review of the Silver Market for 1932*.

of silver have a serious deflationary effect on China's internal price level.[58]

THE CASE FOR DOLLAR DEPRECIATION

Fundamentally, the purpose of the Administration's later monetary moves was the same as that of its earlier abandonment of the gold standard. It was felt that commodity prices must be raised in order to stimulate business activity and hasten re-employment, and as a means to reduce the crushing burden of indebtedness. The deflationary process of the previous four years, with its drastic reduction of wages, prices and profits, had brought business activity almost to a standstill, greatly intensified the real burden of debt and thereby brought the entire credit structure to the verge of collapse. In correcting this situation, either one of two divergent courses could have been adopted. First, debts might have been adjusted to the prevailing level of prices by reducing the face value of existing contractual obligations. Second, monetary measures might have been taken to expand purchasing power and stabilize prices at a higher level. As attempts to follow the first course had proved disastrous under the Hoover Administration, President Roosevelt chose the second of these alternatives and, by threat of currency inflation, had provoked a substantial rise in prices. When the beneficial effects of this move were threatened late in October through an undesired increase in the exchange value of the dollar, some argued that it was necessary for the United States to control the external value of its currency.[59] A few Administration supporters went so far as to assert that the commodity price level could be raised only "if it is impossible for foreigners to buy gold and sell gold at will, thus determining the price and with it the value of the dollar."[60] A return to the gold standard at a new parity was considered inadvisable as there was no way of determining the exact price level which would result from any given revaluation of the dollar. Therefore, it was proposed to adjust the gold value of the dollar by the process of trial and error in order to discover what value would support a level of prices approximately equivalent to that prevailing in 1926. By this means, it was claimed, the United States might obtain a general rise in prices without assuming the risks involved in direct currency inflation. Roughly, the process of control was similar to that utilized by the British Equalization Fund, with this difference—British control was exercised through the purchase and sale of foreign exchange, while the United States at first limited itself to the purchase of gold.

In the absence of an authoritative statement by the Administration as to the manner in which this device might be expected to influence prices, two divergent and somewhat contradictory theories have been advanced. According to the simpler of these, gold standard currencies derive their value from the worth of gold as a commodity.[61] Hence, reducing the gold value of a currency must ultimately cut its purchasing power in the form of all commodities by a proportionate amount. One finds essentially the same view, stated more specifically, in a frequently used metaphor which pictures the United States applying the lever of exchange depreciation against the fulcrum of the world's gold price level as a means to lift the American internal price level.[62] The alternative explanation rests on the fact that a depreciated currency acts as a stimulus to exports and a barrier to imports, thus directly aiding the American producer and ultimately bringing a compensating adjustment in prices. While these objectives appear to conflict, it is possible for each to be partially attained through a moderate advance in prices which would not entirely wipe out the differential favoring American products.

THE CASE AGAINST THE GOLD POLICY

Critics of the Administration's program do not wholly deny the validity of this line of reasoning, but declare that there is no assurance that either goal can be attained or, if achieved, that either will bring the supposed benefits. Very few economists, for example, accept in its entirety the theory that the value of money rests directly on the commodity value of gold, holding it to be more nearly accurate to say that the monetary demands for gold determine its commercial worth.[63] The extreme complexity of modern economic activity makes it impossible to predict the effect of changes that are confined to monetary factors alone.[64] Under the circumstances, therefore, it is difficult to say whether the cheapening of the dollar in terms of gold will stimulate domestic prices, or merely lead to an advance in the world value of gold in terms of commodities, which will leave dollar prices stationary. While a small country with a relatively large foreign trade could alter the gold content of its currency without greatly affecting external prices and could thereby obtain the full effect of devaluation,[65] it is plain that a change in value of the cur-

58. Cf. *New York Times*, December 11, 1933.

59. Walter Lippmann, "Toward a Managed Currency," *New York Herald Tribune*, October 24, 1933.

60. R. G. Tugwell, "New Monetary Policy Regarded Logical Step," *The Sunday Star* (Washington), November 5, 1933.

61. George F. Warren, "Is our Gold Standard too Rigid?" *The Forum and Century*, April 1933, p. 176.

62. "American Recovery and the Dollar," *The Bulletin of International News*, November 23, 1933.

63. Cf. R. G. Hawtrey, *The Gold Standard in Theory and Practice* (New York, Longmans, 1931), p. 47-49.

64. Cf. Leo Pasvolsky, *Current Monetary Issues* (Washington, Brookings Institution, 1933), p. 119-26.

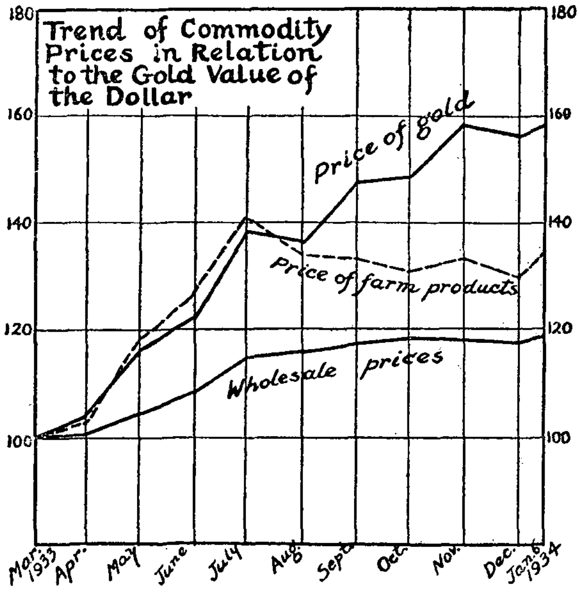
65. Cf. B. M. Anderson, "On the Practical Impossibility of a Commodity Dollar," *The Chase Economic Bulletin, 1933*, Appendix A.

rency of a country occupying as predominant a position in world trade as the United States must react on external prices nearly, if not fully, as much as on domestic prices. This possibility is accentuated by the fact that the American price level is less sensitive than that of most countries, due to the relatively small proportion of American goods entering into foreign trade.[66] Furthermore, in the absence of widespread distrust of money as such, some authorities see little reason to believe that mere depreciation of currency can bring a general rise in prices at a time of acute business depression when consumer purchasing power is at its lowest ebb.[67]

The trend of American prices since October 22, critics aver, bears out this contention. While it is admitted that the Administration's gold policy has not been in operation long enough to justify a definitive analysis of its effectiveness, it appears to have had practically no influence thus far on the price level. Even farm prices, which are exceptionally volatile, advanced but slightly. The price of imported commodities responded in full to the increased cost of foreign exchange, but—contrary to theory—the commodities which the United States exports rose but slightly.[68] By the end of December the index of wholesale prices had returned to exactly the level it occupied at its low point on October 21.[69] An examination of the chart below indicates that while prices followed the trend of the dollar rather closely at first, the relationship became less marked with each succeeding month.

Dollar Depreciation and the Export Market

The failure of American prices to rise in proportion to the decline of the dollar is generally believed by Administration supporters to be temporary. Meanwhile, it is claimed



that this country should benefit materially from the relative advantage given to domestic producers in the markets of the world by the low American price level. That such an advantage exists during the transitional period before costs become fully adjusted to the new price level is unquestioned.[70] While there has been a slight increase in wages as the result of the industrial codes under the N.R.A., costs of production as a whole, chiefly wages, have by no means kept pace with the declining dollar.[71] Whether this apparent gain for American producers is beneficial to the country as a whole is seriously questioned by many authorities. At best the favorable position is a temporary one. If depreciation is checked within reasonable limits, an adjustment soon ensues either through a rise in domestic costs or a decline in the world price level. On the other hand, if depreciation is continuous, as was the case in the German inflation, the exchange advantage is soon offset by an increasing instability and uncertainty in concluding contracts. Moreover, even in the initial stages of depreciation when the theoretical advantage of the domestic producer is the greatest, other factors frequently outweigh that of cheapened currency. Prior to the suspension of the gold standard in the United States, an investigation conducted by the Tariff Commission showed that between October 1931 and February 1932 the imports from six leading European countries which were off the gold standard declined more than the imports from six other European countries which had retained gold as a basis for their currencies. The same was also true of non-European countries which had abandoned gold.[72]

The foreign trade statistics of the United States during the first few months after departure from gold also stand in complete contradiction to the above theory. During the three summer months, when inflationary sentiment was at its height, the United States had an import surplus for the first time in many years. Two possible explanations have been offered for this unexpected development: (1) that the depreciation of the dollar led domestic consumers to stock up on imported goods as a protection against further decline in American currency, while many

66. Cf. Charles O. Hardy, *Devaluation of the Dollar* (Public Policy Pamphlet No. 8, University of Chicago Press, 1933), p. 21.
67. Cf. statement by O. M. W. Sprague upon resignation of his post as special financial adviser to the Treasury, *New York Times*, November 22, 1933.
68. Cf. *New York Herald Tribune*, December 11, 12, 1933.
69. On October 21 and December 23 the index of wholesale prices was 70.4; on the latter date the index of farm prices was 54.8 as compared with 54.2 on October 21.
70. Cf. F. W. Taussig, *International Trade* (New York, Macmillan, 1927), p. 346-50.
71. For estimate of increased labor costs under the N.R.A., cf. *Standard Trade and Security*, Vol. 69, No. 39, Section 1, September 29, 1933.
72. *Depreciated Exchange* (Washington, U. S. Tariff Commission, Report No. 44, Second Series, 1932), p. 1-2; cf. also W. O. Scroggs, "Depreciated Currencies and World Trade," *Foreign Affairs*, April 1933.

foreigners postponed purchase of American products in the belief that they would be able to obtain them cheaper at a later date; (2) that the exceptional spurt in industrial activity which resulted from the fear of impending inflation necessitated the importation of exceptionally large stocks of raw materials from abroad. Beginning with September, American foreign trade became more normal in character, with imports playing a relatively less important rôle. By the end of the year there were clear-cut indications that dollar depreciation was acting as a stimulus to exports, although in gold value the 1933 figures showed a marked falling off from those of the corresponding months of 1932.

UNITED STATES FOREIGN TRADE
(in millions of dollars)

Month	Dollar Value 1932	Dollar Value 1933	Percent of Change	Gold Value 1933	Percent of Change
EXPORTS					
Feb.	154	102	−34	102	−34
Mar.	155	108	−31	108	−31
April ..	135	105	−22	101	−25
May	132	114	−13	98	−25
June ..	114	120	+ 5	98	−14
July	107	144	+35	104	− 3
Aug.	109	131	+21	96	−12
Sept. ..	132	160	+21	109	−17
Oct.	153	194	+27	131	−14
Nov.	139	184	+32	116	−17
IMPORTS					
Feb.	131	84	−36	84	−36
Mar.	131	95	−28	95	−28
April ..	127	88	−30	84	−34
May	112	107	− 5	92	−18
June	110	122	+11	100	− 9
July	79	143	+80	103	+29
Aug.	91	155	+70	114	+25
Sept. ..	98	147	+49	101	+ 3
Oct.	105	151	+44	103	− 2
Nov.	104	128	+23	81	−22

Viewed from a larger angle, moreover, many economists question the advisability of action by the United States which seeks to improve its balance of trade by monetary methods. While abandonment of the gold standard has frequently given substantial relief to harassed debtor countries, the United States—as one of the world's principal creditor nations possessing normally a favorable balance of trade—is in a very different position. If its vast foreign investments are to yield a return, it is clear that some means of payment must be afforded. This can be done only through a contraction of exports, permitting an import surplus; or, if exports are to be maintained at the present level, through considerable expansion of imports.[73] From this point of view, at least, the necessary adjustments of American commercial policy would appear to be the direct opposite of those brought about by the present monetary program. On the other hand, certain observers maintain that under the capitalist system it is necessary for a creditor country to dispose of its surplus production on foreign markets.[74] Since a resumption of foreign lending is impossible at the moment, the depreciation of the dollar, having the same effect, may be defended as essential for the restoration of prosperity.

EFFECT OF POLICY ON FOREIGN COUNTRIES

In the final analysis, most authorities would agree that in view of the fact of world interdependence the success of the government's monetary policy turns on its effect on world economic conditions. On what this effect will be, as on the factors thus far discussed, there is a wide difference of opinion. Some would concur with the President in asserting that any policy which would bring a genuine recovery to the United States would inevitably prove of great benefit to all countries as a result of a revival in American demand for supplies.[75] The majority of foreign observers believe that unless American prices are raised to the full extent of dollar depreciation, the policy is bound to prove injurious to the outside world. Any form of commercial uncertainty is necessarily damaging to international trade, and therefore to the principal trading nations.[76] Moreover, while the absorption of gold from foreign countries is not one of the objectives of the Administration's program, there is a strong possibility that in order to make the policy effective a considerable amount of gold may have to be purchased—which will seriously undermine the reserves of such countries as are still on the gold standard.[77] Whether this would of necessity drive France off gold is by no means certain, but the positions of Holland, Switzerland and Belgium are clearly precarious. If the currencies of these countries are forced from the gold standard by pressure from the American dollar, they would undoubtedly fall to a substantial discount, and the United States would be immediately bereft of the advantages it set out to obtain. There is a further possibility that sterling and the other currencies already independent of gold would be allowed to fall in sympathy with the decline of the dollar, in which case there would be grave danger of a "currency war" involving all the evils of uncontrolled inflation and greatly accentuating international animosities. At the very least, European inflation would entail drastic political readjustments of a far-reaching character.

Moreover, while the advantages accruing to American exporters from an undervalued

73. For fuller development of this view, cf. Stewart, "American Commercial Policy and the World Crisis," cited.

74. Cf. J. Strachey, "The Two Wings of the Blue Eagle," *The Nation*, January 10, 1934, p. 43.

75. Cf. R. G. Hawtrey, *Trade Depression and the Way Out* (New York, Longmans, new edition, 1933), p. 167-72; also *Midland Bank Monthly Review*, July-August, 1933, p. 6.

76. Cf. *The Economist*, November 18, 1933, p. 949.

77. Cf. *Bulletin of International News*, November 23, 1933, p. 9-10.

dollar may easily be exaggerated, foreign nations are bound to resent a persistent and relentless offer of cheap American supplies, unaccompanied by a proportionate increase in its demand for foreign products.[78] Just how harmful this will be to foreign countries depends on a number of factors. It has been estimated, for instance, that although the "purchasing power parity" between the dollar and the pound is now approximately $4.30, Great Britain stands to lose comparatively little from American competition because at least two-thirds of all British exports are non-competitive with those of the United States.[79] The longer the period in which the bounty for American exports persists, however, the greater the possibility of competition in fields not now considered.[80] From the standpoint of foreign nations, competition with a depreciated dollar is feared not so much because of the danger of an actual transference of markets, but because of the continuous depressing influence which would be exerted on world prices. Already competent observers are asserting that economic recovery in the world as a whole has been increasingly hampered by the deflationary effect of dollar depreciation.[81] Whatever the cause or causes, it is evident from the following table that the trend toward rising prices throughout the world during the late spring and early summer has been definitely checked, and a renewal of deflationary tendencies may be observed in recent months. Of the eleven countries listed, eight enjoyed an increase in prices between January and July, and nine suffered declining prices between July and October. This decline continued unchecked through November in seven of the eleven countries.

INDEX OF WHOLESALE PRICES IN CERTAIN FOREIGN COUNTRIES — 1933[82]

	Jan.	*July*	*Oct.*	*Nov.*
Belgium	521	506	489	485
Canada	63.9	70.5	67.9	68.7
Czechoslovakia	96.6	98.3	96.2	95.7
France	390	397	384	383
Germany	91.0	93.9	95.7	96.1
Italy	296	283	277	275
Japan	139.8	137.6	136	135
Poland	56.3	58.2	54.4	54.3
Sweden	106	108	109	110
Switzerland	91.3	91.7	90.7	91.0
United Kingdom	61.2	65.3	64.0	63.1

Despite the threat of a devastating currency war, critics admit that there would be much to justify the government in its present policies if they were essential to the restoration of national prosperity. But it is claimed that the supposed dilemma involving a choice between depreciation of the dollar and continuation of domestic deflation does not actually exist. "Reflationary" action can be achieved without adverse international repercussions by means of large-scale government expenditures. Instead of injuring the outside world through a diminished demand for foreign goods, a large public works program would greatly increase the demand for imports and thus tend to raise world prices.[83]

Threat of Retaliatory Action

Should American monetary policy either through continued gold purchases or devaluation, continue to exercise a depressing effect on world prices, foreign nations will obviously be forced to adopt defensive measures against the challenge of the cheapened dollar—thereby adding materially to the already excessive trade barriers created in recent years by the rising tide of economic nationalism. Just what form these retaliatory measures will take and how seriously they will react on American economic activity, it is impossible to predict. As flat tariff increases have proved an inadequate protection against a rapidly declining currency, the most widely used protective device is the imposition of a surtax equal to the differential between current exchange rates and the par value of the depreciated currency. At present three important trading countries have regulations on their statute books providing for the imposition of a surtax which could be applied to imports from the United States, but to date none is collecting the additional duty.[84] Recent years have also seen the development of various forms of quantitative trade regulation, such as the quota system, which if properly administered furnish a still more complete protection against depreciating currencies. A third and even more powerful weapon of defense, which foreign countries have so far been extremely loath to use, is that of competitive currency depreciation. With all but a few countries having already abandoned the gold standard, it is to be expected that the forced depreciation of the dollar will be accompanied by a corresponding drop in the gold value of all paper currencies.[85] Although all responsible British authorities believe that extension of the present currency warfare would be disastrous,[86] the fact that the decline of sterling has not been greater to date[87] is probably due primarily to the extraordinary influx of capital into

78. For theoretical discussion of currency depreciation as a means of price stimulation, cf. R. F. Harrod, *International Economics* (New York, Harcourt, Brace, 1933), p. 153-5.
79. For detailed figures, cf. *The Economist*, November 25, 1933, p. 1003-4.
80. Cf. *ibid.*
81. *Ibid.*, Trade Supplement, November 25, 1933.
82. Cf. *Prices and Price Indexes*, December 1933, Dominion Bureau of Statistics, Ottawa, Canada; and *The Analyist*, December 23, 1933.
83. Harrod, *International Economics*, cited, p. 155; J. M. Keynes, *The Means to Prosperity* (New York, Harcourt, Brace, 1933), p. 25-26.
84. France, Italy and Canada. (Cf. *Commerce Reports*, June 17, September 30, December 2, 16, 1933.)
85. Einzig, *The Sterling-Dollar-Franc Tangle*, cited, p. 157.
86. Sterling declined about 5 per cent in terms of gold between April 19 and December 15, 1933.
87. Cf. *The Economist*, November 4, 18, 1933.

London rather than to concerted attempts to bolster the value of the pound. While it is possible that the United Kingdom will rely on the tariff as a means of withstanding the pressure of the dollar,[88] many debtor countries have been put into a much more difficult position. Argentina's recent action in "unpegging" the peso is asserted to be at least partially due to the cheapened dollar.[89]

MANAGED CURRENCY AND ECONOMIC NATIONALISM

Back of the controversy over the Administration's immediate program lies the even more fundamental one of permanent policy raised by the proposal "to establish and maintain a dollar which will not change in its purchasing power during the succeeding generation."[90] For years economists have disputed the possibility of devising a means to eliminate price fluctuations. It is probably accurate to say that a majority believe that some form of monetary control over the price level is both possible and desirable, although they differ widely as to how it can best be accomplished. There are others who contend that price stabilization by any means is wholly impractical and that efforts to achieve this end can only add to existing economic confusion.[91] Those who would regulate prices by monetary or credit manipulation differ not only as to method, but as to the degree of stabilization that is practicable. It is possible for central banks, for instance, to exercise a fairly effective control over prices through manipulation of the rediscount rate and open-market operations while remaining on the gold standard.[92] But such control would not eliminate the long-term swings in the value of gold itself, and therefore could not assure a stable price level over a period of years. The effort to regulate a nation's prices by independent monetary action, moreover, is clearly inconsistent with the stability of the foreign exchanges.[93]

THE NEED OF AN INTERNATIONAL STANDARD

Many monetary experts sharply dispute the Administration's contention that elimination of fluctuations in the domestic price level is of greater importance than stability of international exchanges. Only through an international monetary standard, they assert, can there be a basis for regulating the reciprocal relations of the nations of the world.[94] To a very large extent the complex economic structure of the modern world has been built on exchange rigidity which permits an international division of labor on the basis of comparative costs. Departure from this principle involves, at the very least, considerable readjustment of national economic activities and, at the worst, the possibility that the industrial or agricultural activities of great sections of a nation's population might be wiped out overnight by monetary manipulations. If used as an aggressive weapon of economic nationalism, currency regulation can be vastly more destructive than tariffs, quotas, or the other more commonly recognized instruments of national aggression. A monetary system managed solely with regard to domestic considerations implies, and to a degree necessitates, a retreat from internationalism in all economic relationships, while reconstruction of a world economy awaits, as a fundamental step, the restoration of exchange stability.[95]

Underlying present currency issues, therefore, lies the basic question of the nature of future world economic organization. If the trend is to be toward the development of a series of self-sufficient national economies,[96] it is obvious that the monetary policies of each country must be dictated solely by domestic considerations. A return to *laissez-faire* internationalism such as prevailed in the nineteenth century, on the other hand, clearly necessitates the restoration of the gold standard under conditions which would assure its efficient functioning.[97] For political reasons, such a step would probably have to be accompanied by a general reduction in the gold content of the various currencies, although international agreement of the new parities would not be easily secured. The establishment of a planned international order, as a third distinct alternative, would necessitate measures for assuring not only rigidity of exchanges, but international price stability. Technically, this presents even more serious difficulties than domestic price regulation, but at least one scheme for achieving this end has won considerable support from leading economists.[98] It is safe to say, however, that no measures can be taken toward monetary stability except through the active cooperation of the two principal trading nations—Great Britain and the United States.[99] *De facto* stabilization of sterling and the dollar, irrespective of whether they are on the gold standard, would necessarily be the first step in that direction.

88. Cf. *New York Times*, December 15, 1933.
89. Cf. *New York Times*, December 1, 1933; *New York Herald Tribune*, December 4, 1933.
90. Cf. p. 274.
91. Cf. Anderson, "On the Practical Impossibility of a Commodity Dollar," cited.
92. *Committee on Finance and Industry (Macmillan Committee) Report* (London, H. M. Stationery Office, 1931), Cmd. 3897, p. 92-99.
93. Cf. Pasvolsky, *Current Monetary Issues*, cited, p. 130-2.
94. Cf. Charles Rist, "Gold and the End of the Depression," *Foreign Affairs*, January 1934.
95. Cf. Pasvolsky, *Current Monetary Issues*, cited, p. 131.
96. For discussion of the feasibility of national self-containment, cf. Stewart, "Tariff Issues before the New Administration," *Foreign Policy Reports*, March 29, 1933.
97. Cf. League of Nations, Monetary and Economic Conference, *The Draft Annotated Agenda*, C.48.M.18.1933.II, p. 7-8, 12-17.
98. Cf. Keynes, *The Means to Prosperity*, cited.
99. Cf. Pasvolsky, *Current Monetary Issues*, cited, p. 132.